

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF CALIFORNIA

McKesson Corp., a Delaware Corp.,
Plaintiff,

No. C-07-5715 WDB

v.

**ORDER AND MEMORANDUM
OPINION RE MCKESSON'S
MOTION FOR SUMMARY
JUDGMENT**

Familymeds Group, Inc., f/k/a
Drugmax, Inc., a Connecticut
corporation,

Defendants.

Familymeds Group, Inc., f/k/a
Drugmax, Inc., a Connecticut
corporation,

Counterclaimant

v.

McKesson Corp., a Delaware
corporation,

Counterdefendant.

INTRODUCTION AND STATEMENT OF FACTS

Pursuant to contract, executed on February 2, 2007, McKesson Corporation was to supply prescription drugs and other health and beauty care products to pharmacies owned and operated by Familymeds Group, Inc., ("FMG"). We refer to this contract as the "Supply Agreement."

1 FMG pharmacies ordered products using McKesson's Supply Management
2 Online computer system ("SMO"). Declaration of Leslie Morgan in Support of
3 Motion for Summary Judgment, filed June 4, 2008, ("Morgan Decl."), at ¶¶4-6.
4 McKesson immediately generated an invoice for each order placed and posted that
5 invoice on the SMO system the following day. *Id.* FMG was able to access and
6 pay its invoices online. *Id.*

7 The Supply Agreement obligates FMG to pay each invoice within seven
8 days of the invoice date. Contracts Filed Under Seal, filed July 22, 2008, Ex. A
9 ("Supply Agreement") at §4A. Moreover, the Supply Agreement requires FMG to
10 pay the amount stated as due on each invoice in full within those seven days even
11 if FMG disputes the amount owing. FMG may pay less than the invoiced amount
12 only if it has secured written authorization from McKesson to do so. The Supply
13 Agreement provides,

14 Customer [FMG] agrees to render payment in full to McKesson on the
15 applicable due date as specified in this Agreement without (i) making
16 any deductions, short payments, or other accounts payable
17 adjustments to such payment obligation; or (ii) seeking to condition
18 such remittance on any demand for or receipt of proofs of delivery.
Any accounts payable adjustments claimed by Customer shall require
prior written authorization of McKesson and must be supported by
accompanying detail documenting the basis for any such requested
adjustments.

19 Supply Agreement at §4F.

20 On November 9, 2007, McKesson filed its Complaint for Breach of Contract
21 alleging that FMG has failed to pay for merchandise sold and delivered under the
22 Supply Agreement. According to McKesson, FMG owes McKesson \$814,419.44
23 for unpaid invoices as well as for late fees and service charges assessed pursuant to
24 the Supply Agreement. Supplemental Declaration of Leslie Morgan, filed August
25 7, 2008, ("Supp. Morgan Decl."), at ¶4.

26 On December 17, 2007, FMG filed counterclaims alleging (1) that the
27 Supply Agreement encompasses an implied obligation for McKesson to provide
28

1 FMG with documentation sufficient to audit the invoices and (2) that, as a matter
2 of equity, FMG is entitled to an accounting. FMG asserts that McKesson has
3 charged FMG prices that exceed those contemplated by the Supply Agreement
4 and/or that accounting methods used by McKesson have resulted in the erroneous
5 assessment of late fees and service charges. Declaration of Edgardo Mercadante in
6 Opposition to Motion for Summary Judgment, filed August 4, 2008, ("Mercadante
7 Decl."); Declaration of Christian Tregillis in Opposition to Motion for Summary
8 Judgment, filed August 4, 2008, ("Tregillis Decl.").¹

9 On June 4, 2008, plaintiff filed its Motion for Summary Judgment. Plaintiff
10 asks the Court to enter judgment in McKesson's favor and against FMG on
11 McKesson's claim that FMG breached the Supply Agreement by failing to pay
12 invoices within seven days and to find that FMG's breach has damaged McKesson
13 in the amount \$814,419.44. McKesson also asks the Court to adjudicate in
14 McKesson's favor FMG's counterclaims for specific performance of an implied
15 obligation to provide an accounting and for an accounting in equity. Motion at 16-
16 21.

17 FMG opposes plaintiff's Motion and asks the Court to enter judgment in
18 FMG's favor with respect to its counterclaims.

19 On August 20, 2008, the Court conducted a hearing in connection with
20 plaintiff's Motion. At the hearing, the Court announced its tentative ruling and
21 provided the parties with two weeks in which to discuss settlement. Having
22 received no notification from the parties that the case has settled, the Court RULES
23 as follows.

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27 ¹Messrs. Mercadante's and Tregillis' declarations have been filed under seal. Defendant
28 e-filed redacted versions of these declarations on July 30, 2008.

STANDARD ON SUMMARY JUDGMENT

To succeed on a motion for summary judgment, the moving party must establish that, under facts that are not subject to genuine dispute, that party is entitled to judgment as a matter of law. Federal Rule of Civil Procedure 56(c). In reviewing a motion for summary judgment, the Court considers the evidence in the light most favorable to the party against whom the judgment is sought.

DISCUSSION

I. Plaintiff's Claim for Breach of Contract

McKesson must demonstrate that there are no material disputes with respect to each of the elements of its breach of contract claim. To establish a claim for breach of contract McKesson must prove that the parties have an enforceable contract, that McKesson performed its obligations thereunder, that FMG breached the contract, and that FMG's breach caused McKesson damages.

A. Elements of Breach of Contract

FMG does not dispute that the Supply Agreement is an enforceable contract or that McKesson performed its obligation to deliver products ordered by FMG pharmacies.²

FMG concedes that sections 4A and 4F of the Supply Agreement provide that FMG was to pay each invoice in full within seven days of the invoice date unless FMG obtained written authorization from McKesson to adjust the amount

²FMG appears to allege that McKesson did not perform its obligation under the Supply Agreement to charge accurate prices. However, as explained *infra*, even if true, pursuant to the terms of the Supply Agreement a failure to perform the obligation to charge accurate prices would not excuse FMG's obligation to pay the invoices by the due date.

1 paid.³ See FMG's Separate Statement of Disputed, Undisputed and Additional
2 Facts, filed August 4, 2008, at No. 5 and 8. Furthermore, FMG does not dispute
3 that, to this day, it has not paid in full at least some of the invoices or obtained
4 written authorization from McKesson to avoid payment on those invoices.
5 Accordingly, it is undisputed that FMG has breached the terms of sections 4A and
6 4F of the Supply Agreement.

7 FMG asks the Court to deny McKesson's motion for summary judgment on
8 the ground that there is a genuine dispute of material fact with respect to damages.
9 Opposition at 8. However, FMG does not appear to contend that it owes
10 McKesson no money. FMG's position is that there is a material dispute about the
11 amount of McKesson's damages. Opposition at 8:25-27. There is, therefore, no
12 dispute that McKesson has demonstrated that it has been damaged by FMG's
13 breach.

14 Accordingly, McKesson has established all four elements of its claim for
15 breach of contract. The Court GRANTS plaintiff's motion for summary
16 adjudication of its claim that FMG breached the Supply Agreement. The Court
17 will enter judgment in McKesson's favor and against FMG for that amount of
18 damages as to which there is no genuine dispute of material fact. Additionally, as
19 explained on the record, at this juncture, entry of judgment is WITHOUT
20 PREJUDICE. McKesson may attempt to prove that FMG owes more than the
21 amount of the incident judgment. Similarly, defendant may attempt to prove that
22 McKesson overcharged FMG during the course of performance and that FMG is,
23 therefore, entitled to a judgment in its favor for established overcharges.

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25 _____
26 ³Mr. Mercadante testifies that the seven day due date applied to less than half of the
27 pharmacies subject to the Supply Agreement. Mercadante Decl., at ¶¶17-19. However, as noted
28 *infra*, at the August 20, 2008, hearing counsel for FMG indicated that FMG concedes that this
provision applied to all invoices regardless of the "type" of pharmacy invoiced.

B. Amount of Damages Not Subject to Genuine Dispute

McKesson asserts that FMG currently owes \$814,419.44.⁴ Supp. Morgan Decl., at ¶4. This amount includes (1) the “gross payments” due from the unpaid invoices,⁵ (2) service charges that are applied to late and unpaid payments at the rate of 1% every 15 days, (3) additional amounts due such as “add-bill” items, and (4) other price adjustments such as credits for products returned by FMG pharmacies. *Id.*; Morgan Decl., at ¶9.

FMG contends that it has identified “significant accounting discrepancies, overcharges, and inconsistencies” that call into question the amount allegedly owed by FMG. Opposition at 1. In an effort to demonstrate that a genuine dispute of material fact exists with respect to the amount of McKesson’s damages, FMG submitted the declarations of Edgardo Mercadante and Christian Tregillis.

Mr. Mercadante is the President, Chief Executive Officer, and Chairman of the Board of FMG. In his declaration he describes various allegedly questionable pricing and/or accounting practices by McKesson that he states he has identified from information provided by McKesson. In Mr. Mercadante’s view, the issues he describes call into question the accuracy of McKesson’s alleged damages. The Court finds that Mr. Mercadante’s declaration is not sufficient, as a matter of law, to establish a genuine issue of material fact as to the amount of damages owed McKesson.

Mr. Mercadante is not qualified to testify on matters of accounting, finance or statistics. Mr. Mercadante functions as a custodian of records for FMG and has substantial experience “in the prescription health care, chain pharmacy and retail nutrition industries.” Mercadante Decl., at ¶3 and Ex. 1. Absent from his

⁴FMG’s debt continues to accrue service charges of 1% every 15 days. Supply Agreement at ¶4E.

⁵Pursuant to the Supply Agreement, FMG received a 2% discount from product prices, as reflected by the “net payment” amount, when it paid an invoice by the due date. If FMG failed to pay an invoice within seven days it would lose this discount and become obligated to pay the undiscounted cost -- the “gross payment” amount. Supply Agreement at ¶4E.

1 declaration are any representations that he has any accounting, statistical, or other
2 financial background.

3 Additionally, even if Mr. Mercadante had the requisite experience, he has
4 not provided the Court with a description of his methodology sufficient to support
5 an inference that his assertions are valid. Mr. Mercadante uses unspecified
6 “market” statistics from what appears to be a trade organization. He also makes
7 the conclusory pronouncement that he tested a “statistically significant” number of
8 McKesson’s invoices without describing how many invoices he tested.

9 It follows that Mr. Mercadante has not proffered competent evidence from
10 which a rational trier of fact could find that there is a genuine dispute regarding the
11 amount FMG owes.

12 We also feel constrained to comment on Mr. Mercadante’s assertion that
13 when the parties entered the Supply Agreement they intended to distinguish
14 between FMG’s “retail” and “non-retail” pharmacies and that the parties did not
15 intend to subject FMG’s fifty “non-retail” pharmacies to the seven day payment
16 requirement. Mercadante Decl., at ¶¶17-19. According to Mr. Mercadante, there
17 is a genuine dispute about the amount of damages owed McKesson because FMG
18 should not have incurred service charges “for [FMG’s] alleged failure to pay
19 within seven (7) days for goods delivered to [FMG’s] non-retail pharmacies.”
20 Mercadante Decl., at ¶19. This assertion (apparently made here for the first time
21 since the inception of the Supply Agreement) is transparently implausible in light
22 of the clear language of the contract and the parties’ course of performance.⁶ The
23 Court finds that no rational trier of fact could credit this testimony. Moreover, the
24 substantial implausibility of this testimony calls into serious question Mr.
25 Mercadante’s credibility and ethics, and this alone serves as a predicate for
26 deeming the entire declaration incompetent.

27
28 ⁶We note that counsel for FMG asserted at the August 20th hearing that FMG now
acknowledges that all invoices were to be paid within seven days. Transcript of August 20,
2008, hearing.

1 The other evidentiary basis for challenging the amount of damages claimed
2 by McKesson is the declaration of Mr. Tregillis. Mr. Tregillis is a Certified Public
3 Accountant with significant experience in forensic accounting and data analysis.
4 Tregillis Decl., at ¶2 and Ex. 1. Having reviewed the unpaid invoices and
5 McKesson's monthly "statement" dated May 30, 2008, Mr. Tregillis testifies that
6 he has identified multiple errors and inconsistencies in the documents used by
7 McKesson to support its damages claim. Tregillis Decl., at ¶¶6-24.

8 McKesson has responded to each asserted error and discrepancy identified
9 by Mr. Tregillis. Supp. Morgan Decl., at ¶¶4-25. At this juncture, the Court will
10 not rule with respect to each asserted error. We note, however, that all but one of
11 McKesson's responses to the categories of charges questioned by Mr. Tregillis
12 appear to explain adequately the documentation supporting McKesson's claim for
13 damages. It is possible that while the documentation indicates that certain products
14 were designated as having been billed under the "Cost Plus" (or "Cost of Goods")
15 pricing method, those items actually were priced as "specially priced
16 merchandise." Tregillis Decl., at ¶9 and Ex. 2; Supp. Morgan Decl., at ¶14;
17 Transcript of August 20, 2008, hearing. Because, on the current record, we cannot
18 find with the requisite certainty that there is no genuine dispute with respect to this
19 category of charges, it is inappropriate to enter judgment with respect to the entire
20 amount of damages sought by McKesson.

21 Nonetheless, as explained at the August 20th hearing, the record supports
22 entry of judgment in favor of McKesson and against FMG in the amount
23 \$747,474.09. The express terms of the contract require FMG to pay the invoiced
24 amounts in full without deductions or adjustments. Supply Agreement at 4F.
25 Moreover, the contract provided a procedure by which FMG could seek to protect
26 itself from pricing or other accounting errors. FMG agreed that any adjustments to
27 the amount it owed McKesson would be made only with prior written authorization
28 from McKesson. *Id.* Therefore, under the express terms of the contract, if FMG

1 did not pay an invoice within seven days and prior to the expiration of the seven
2 days it had not sought and received written authorization from McKesson not to
3 pay, then FMG breached the Supply Agreement and acquired a duty to pay the
4 invoiced amount.

5 The evidence supports a finding that the amount invoiced and, therefore, the
6 amount that, absent prior written authorization from McKesson, FMG had a duty to
7 pay within seven days regardless of any possible errors, is \$747,474.09.⁷ Supp.
8 Morgan Decl., at ¶5; Supp. Schrank Decl., at ¶15. This amount represents the “net
9 price” due and payable within seven days from the unpaid invoices as opposed to
10 the 2% larger “gross price” payable when payment is not made by the due date.
11 FMG has not demonstrated any factual basis for disputing that this amount was
12 invoiced and was due and payable on the relevant due dates by virtue of the fact
13 that FMG did not obtain prior written authorization to withhold payment. There
14 has been no proffer that FMG ever sought permission to withhold payment under
15 section 4F or otherwise complained about the billed amounts until September
16 2007, after McKesson ceased shipping products to FMG.⁸ Accordingly, unless and
17 until FMG proves that there are actual errors in McKesson’s unpaid invoices FMG
18 is obligated to remit, at a minimum, \$747,474.09.

21
22 ⁷Although the current record might support an inference that McKesson mislabeled the
23 pricing method used with respect to some forty eight items identified by Mr. Tregillis, it
24 currently does not support an inference that McKesson overcharged for the items. Stated another
way, a rational trier of fact could find that McKesson’s documentation listed the wrong pricing
method, but, on this record, could not find that the actual price charged was the wrong price.

25 ⁸Mr. Mercadante testifies that “during the course of the First Amendment and Supply
26 Agreement, Familymeds made repeated inquiries to McKesson about pricing discrepancies, at
27 multiple levels, as part of its regular and ordinary business routine, practice, habit, process and
28 procedure.” Mercadante Decl., at ¶24. Mr. Mercadante’s testimony fails to create a genuine
dispute of material fact. He does not identify any specific instance in which FMG made such
an inquiry. Similarly, he does not attach any correspondence evidencing these alleged inquiries
and does not identify the person who made the inquiry, the subject matter of the inquiry, or the
date on which it was made. Furthermore, as explained supra, the Court has significant doubts
about Mr. Mercadante’s credibility.

1 Mr. Mercadante represents himself to be a sophisticated businessman in this
2 arena. He was responsible for negotiating the Supply Agreement, and these are the
3 terms to which he agreed.

4 The Court enters judgment in favor of McKesson and against FMG in the
5 amount \$747,474.09 without prejudice to either party's ability to prove that a
6 subsequent judgment is warranted in that party's favor.

7 8 **II. Defendant's Counterclaims**

9 The Court DENIES without prejudice each party's request to enter judgment
10 in its favor with respect to FMG's counterclaims.

11 As indicated on the record, the Court will permit FMG to amend its counter
12 complaint to assert a claim for breach of contract alleging McKesson failed to
13 charge accurate prices if FMG can do so consistent with Federal Rule of Civil
14 Procedure 11. At least some of the information defendant seeks might be obtained
15 through appropriate discovery in the event FMG amends its counter-complaint to
16 assert such a claim. Accordingly, it is premature to rule with respect to the
17 viability of FMG's specific performance and accounting claims.

18 Additionally, even if either of FMG's current counterclaims is viable as a
19 matter of legal theory, FMG has failed to proffer evidence of potential pricing or
20 accounting errors of sufficient scale to justify an accounting of the magnitude FMG
21 seeks.

22 Therefore, neither party is entitled to summary judgment or equitable relief
23 on these claims at this juncture.

24 25 **CONCLUSION**

26 For the reasons stated above and on the record at the hearing on August 20,
27 2008, the Court GRANTS in part and DENIES in part McKesson's Motion for
28 Summary Judgment.

1 The Court GRANTS McKesson's motion for summary adjudication of its
2 claim for breach of contract and will enter judgment in the amount \$747,474.09 in
3 favor of plaintiff and against defendant.

4 The Court enters judgment WITHOUT PREJUDICE to either party's ability
5 to seek a subsequent judgment in its favor.

6 The Court DENIES both parties' requests to rule with respect to FMG's
7 counterclaims for specific performance and for an accounting.

8 **On September 17, 2008, at 3:00 p.m.**, the Court will conduct a case
9 management conference in order to determine how to proceed with the parties'
10 remaining allegations.

11 IT IS SO ORDERED AND ADJUDGED.

12 Dated: September 9, 2008

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14 WAYNE D. BRAZIL
United States Magistrate Judge

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